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1 UNITED STATES DISTRICT COURT  
2 SOUTHERN DISTRICT OF NEW YORK  
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3 SECURITIES AND EXCHANGE  
4 COMMISSION,

Plaintiff,

v.

15 Civ. 894 (WHP)

6 CALEDONIAN BANK, LTD. and  
7 VERDMONT CAPITAL, S.A. *et al.*,

8 Defendants.  
9 -----x

10 March 16, 2016  
11 3:10 p.m.

Before:

12 HON. JAMES L. COTT,

13 Magistrate Judge

14 APPEARANCES

15 U.S. SECURITIES AND EXCHANGE COMMISSION  
16 BY: PATRICK R. COSTELLO  
DEREK S. BENTSEN  
DAVID STOELTING

17 CARTER, LEDYARD & MILBURN, LLP  
18 Attorneys for Defendant Vermont Capital, S.A.  
19 BY: ROBERT A. ZITO  
MARK R. ZANCOLLI

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1 (Case called)

2 THE DEPUTY CLERK: Counsel, state your name for the  
3 record.

4 MR. COSTELLO: Good afternoon, your Honor. Patrick  
5 Costello on behalf of the SEC.

6 THE COURT: Good afternoon, Mr. Costello.

7 MR. BENTSEN: Good afternoon, your Honor. Derek  
8 Bentsen on behalf of the SEC.

9 THE COURT: Good afternoon, Mr. Bentsen.

10 MR. STOELTING: Good afternoon. David Stoelting for  
11 the SEC.

12 THE COURT: Good afternoon, Mr. Stoelting.

13 MR. ZITO: Good afternoon, your Honor. Robert Zito of  
14 Carter Ledyard for Verdmont Capital.

15 THE COURT: Good afternoon, Mr. Zito.

16 MR. ZANCOLLI: Good afternoon. Mark Zancolli from  
17 Carter Ledyard for Verdmont Capital.

18 THE COURT: Good afternoon, Mr. Zancolli.

19 You may all be seated. Let me tell you all how I have  
20 been thinking about this.

21 I have read all of the submissions including the  
22 letter Mr. Zito sent today and that's probably where we should  
23 start, but I like to be practical with discovery disputes.  
24 This is a complicated dispute. The threshold question,  
25 obviously, is whether the information that's being sought is

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1 relevant, either with respect to the SEC's establishment of the  
2 prima facie case with respect to the Section 5 violation or  
3 with respect to Verdmont's defenses and we can talk about that  
4 and maybe we will and/or is it also relevant to the issue of  
5 joint and several liability and we can talk about that. Maybe  
6 we will.

7 Let's assume for the moment that the threshold issue  
8 of relevance is one that I am satisfied requires the Court to  
9 consider the more complicated question here which is whether  
10 Panamanian law forecloses production. But, before we get to  
11 that question, it seems to me that the Court doesn't have to  
12 reach it if, in fact, as the SEC has represented, it can get  
13 the documents from the Panamanian regulatory authorities and  
14 Verdmont certifies that the documents that the SMV would be  
15 providing are in fact the same as what they would otherwise  
16 have been able to get from Verdmont. The issue with respect to  
17 that, it seems to me, is there is an uncertain timeline  
18 associated with that and you have a discovery cutoff date of  
19 April 30th.

20 I am also a little perplexed by the fact that, at  
21 least if I am remembering what I read in the record, that the  
22 SEC did not make at least a formal request of the SMV until  
23 February 24th of this year, notwithstanding that these document  
24 requests were made in the spring of last year at the latest.

25 So, that's another question I have, why was there a

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1 delay. And from the representations Mr. Zito has made to me  
2 both in his declaration of a week or so ago and in the letter  
3 dated today, I need, I think, to get a better understanding  
4 both with respect to what relationship, if any, the SEC has  
5 with Panamanian regulatory authorities and what information is  
6 already in the SEC's possession that it received from Canadian  
7 regulatory authorities. If we go down that path and we  
8 conclude that there is a realistic and rational way for the SEC  
9 to obtain, on a relatively timely basis the outstanding  
10 materials, and that's another question I had which is what in  
11 fact does remain to be produced that the SEC does not already  
12 have, then it seems to me I don't have to get into the thick of  
13 it whether, number one, a United States Court's order fits  
14 within the Panamanian legal framework which I think is a  
15 complicated question; and two, I don't have to consider the  
16 comity factors which also, it seems to me in this case, is a  
17 pretty complicated analysis which I have given thought to, by  
18 the way, but as is always true, if you can resolve something  
19 without reaching the hard legal questions, one should do that.

20 So, that's the framework that I'm bringing here.  
21 Obviously if you think I am misunderstanding or misstating  
22 anything, I obviously need to be educated. You all have lived  
23 with this case far longer than I have and Judge Pauley has  
24 effectively asked me to parachute in because he is otherwise  
25 engaged to deal with this discrete but complex issue.

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1           So, Mr. Mr. Costello, let me start with you. I have  
2 identified a number of questions that I have, let's start with  
3 the letter I got from Mr. Zito today. I assume, in part, the  
4 SEC will tell me that you do not have a formal bilateral  
5 agreement. I don't know if that's a semantic distinction  
6 between what may exist since Mr. Zito is operating under the  
7 assumption that there is what we will call a memorandum of  
8 understanding. That's what he refers to it as in his letter.  
9 Maybe a memorandum of understanding is not a formal bilateral  
10 agreement.

11           So, can you answer, first of all, whether there is at  
12 least a memorandum of understanding?

13           MR. ZITO: Your Honor?

14           THE COURT: You are not Mr. Costello.

15           MR. ZITO: Your Honor, can we go off the record? This  
16 is a very sensitive issue and I just want to inform the Court  
17 of certain sensitive facts I received on my way to the court  
18 house regarding this issue.

19           THE COURT: All right. And you want to go off the  
20 record?

21           MR. ZITO: Yes, your Honor.

22           THE COURT: All right, we will go off the record for a  
23 minute.

24           (Discussion off record)

25           THE COURT: Let's go back on the record.

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1 All right, Mr. Costello.

2 MR. COSTELLO: Thank you, your Honor.

3 Just to give your Honor a little bit of context here,  
4 in terms of agreements that the SEC has with foreign  
5 regulators, those agreements can take one of three forms, as I  
6 am told by my Office of International Affairs -- one is a  
7 treaty, two is a formal bilateral agreement, and three is a  
8 memorandum of understanding/access request.

9 It is really not necessary, I don't think, to get into  
10 the nuances of what one is and one isn't and what have you  
11 because I think once we relate it back to this discovery  
12 dispute we will see that at the end of the day it doesn't  
13 really matter.

14 And so, I will apprise the Court of a little bit of  
15 the time frame here. There has never been a formal bilateral  
16 agreement or a treaty, as I understand it, for the type of  
17 dispute or enforcement action that we have here between the  
18 United States and Panama. Now, that is unlike other regulators  
19 around the world but between the United States and Panama or  
20 the SEC and the Panamanian regulator, no such thing has ever  
21 existed.

22 Recently, within the last few months, there have been  
23 discussions between the SEC and the Panamanian regulator even  
24 though I can't go into the substance of those discussions  
25 because they're confidential, but suffice to say that the SEC

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1 and the SMV have reached a memorandum of understanding/access  
2 request, whatever you want to call it, but I am just pointing  
3 out that it is not one of the first two categories, it is the  
4 third category.

5 Now, the important thing here is that we have asked  
6 the Panamanian regulator to produce, if they have it, the very  
7 same documents that we have sought from Vermont here, and  
8 those are the 10 categories of documents that we have in all of  
9 our filings. So, we have asked them for the very same  
10 information that we are seeking from Vermont.

11 Now, I will get into the mechanics of that in a minute  
12 but I just want to clarify something for the Court. I don't  
13 know what Mr. Zito may have been referring to in terms of the  
14 time frame on this but, as I said, that agreement with the  
15 regulator was reached only recently and we made a request for  
16 these particular categories of documents only recently, and the  
17 reason that we did that only recently is because there never  
18 was any kind of an arrangement with the regulator back when  
19 this case was filed last year. Had there been such an  
20 arrangement then perhaps we could have requested it at that  
21 point in time but there was nothing.

22 Now, why there was nothing I can't speak to that, your  
23 Honor. I'm not involved in negotiations with the Panamanian  
24 regulator, our Office of International Affairs handled that but  
25 I can now tell the Court that there is an understanding with

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1 respect to the information that is in this case.

2 THE COURT: Why couldn't the SEC have made a request  
3 of the Panamanian regulator last spring even before there was  
4 any kind of agreement in the form of an MOU or any other form?

5 MR. COSTELLO: Your Honor, all I can say is that there  
6 was no mechanism in place to make that request. The history as  
7 to how the regulators interact with one another, I don't really  
8 know what the history is. All I can tell you is that there  
9 never was any kind of an arrangement or communication or even  
10 any kind of discourse at the time that this happened. How it  
11 came about that things changed recently, I can't go into the  
12 substantive and in truth, your Honor, I really don't know how  
13 that came about but all I can tell the Court is that now there  
14 is a framework in place that didn't exist before.

15 THE COURT: And is the fact that there is an MOU  
16 sensitive enough that I should be sealing this transcript, at  
17 least with respect to the discussion about it? Or not so much.

18 MR. COSTELLO: No, your Honor, it is not necessary to  
19 seal it about the substance of it but, suffice to say, that in  
20 this context, just to bring the Court up to speed on what  
21 happened, as we understand it, Vermont had made a request of  
22 the SMV for the letter agreement or the memorandum of  
23 understanding that exists between the two regulatory agencies  
24 last week. The SMV then responded to Vermont, as we  
25 understand it, and told them that under Rule 5-2015 of the



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1 Panamanian Securities Provisions or what have you, the  
2 existence of or contents of the letter between the regulatory  
3 agencies is confidential, an interregulatory agreement. I'm  
4 not quite sure of what the term is in Panama. But, to bring  
5 that back stateside, your Honor, under Section 24(d) of the  
6 Exchange Act, when you have these arrangements between the SEC  
7 and foreign regulators, particularly where the foreign  
8 regulator asks that the contents of the agreement and the  
9 specific terms of it be kept confidential as the SMV has  
10 designated here, the SEC will respect that foreign regulator's  
11 request.

12 And, again, I want the Court just to kind of bring  
13 this into context here as to what this really means. I frankly  
14 don't see how the history of this, the terms of this, the  
15 specifics of this, who signed it, when that happened, all of  
16 that, that doesn't really concern the particular dispute that  
17 we have here. I think that I can represent to the Court, if  
18 that's the concern from Vermont's side, I can represent to the  
19 Court that we have asked the SMV for the very same information  
20 that we have asked from Vermont.

21 THE COURT: And you asked on February 24th?

22 MR. COSTELLO: That was when the actual request itself  
23 was made.

24 THE COURT: And what can you tell me about the  
25 timeline related to any response you expect to get, if

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1 anything? And maybe you can't, but whatever you can say in  
2 that regard I think is of critical importance here.

3 MR. COSTELLO: Certainly, your Honor.

4 I can tell you that the SMF has acknowledged receipt  
5 of the request but my Office of International Affairs has  
6 informed me that they just don't have a sense, given that there  
7 has really been no history to point to unlike other regulators  
8 where we can say, oh, typically this takes a month or two  
9 months. We don't have that here. So, what I can try to offer  
10 the Court is perhaps an alternative to this, if maybe this is  
11 the way the Court wants to go here.

12 We have no problem with trying to run this down with  
13 the SMV. We have no problem with trying to get the information  
14 from them first, we will collect it, we will review it, the  
15 Court can have another status conference, we can talk about it,  
16 we can do whatever that is. My concern is that this is not  
17 going to happen before April 30th. So, what I might suggest as  
18 an alternative, if the Court is interested, if the Court would  
19 be willing to push back that deadline -- and I'm not sure if  
20 that would be a discussion that would need to be had with Judge  
21 Pauley, I imagine it would be -- but, in light of the  
22 circumstances here and in light of keeping in mind the comity  
23 factors and the sensitivities of Panamanian secrecy and what  
24 have you and, again, to paraphrase your Honor from earlier,  
25 maybe we can resolve this on the easier side rather than having

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1 to get into the complicated side, maybe in light of all of that  
2 it would be best, in this instance, to push the discovery  
3 deadline back. That would give us enough time to get the  
4 documents from the regulator, that would alleviate or moot the  
5 need for the Court to engage in any kind of a complicated  
6 analysis, and then would allow us the opportunity to again, as  
7 I believe Vermont's liquidator has represented in one of her  
8 declarations, that she would be willing to sign off on whether  
9 the production is complete or what have you. We can deal with  
10 that down the road.

11 And then I would say what we could do in that  
12 situation is we can see what the SMV has because truthfully we  
13 don't know. And I know Vermont has represented in its filings  
14 that they have given everything to the SMV but I can't verify  
15 that until I actually see what the SMV gives us if they even  
16 are.

17 That's not a guarantee, your Honor. I want to put  
18 that on the record too.

19 THE COURT: What is not a guarantee?

20 MR. COSTELLO: It is not a guarantee that the SMV will  
21 give us this information. We don't have any kind of assurance  
22 that they will. We have asked them for it. We have no  
23 mechanism or means to force them to do anything because they're  
24 a foreign regulatory body, they can do what they please. We  
25 are hoping that they will give us this information.

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1 THE COURT: Well, if there is a memorandum of  
2 understanding what are you understanding? Isn't it that you  
3 are going to share information, as appropriate? You mean in  
4 these circumstances they might say it is not appropriate to  
5 give you this information for some reason?

6 MR. COSTELLO: Precisely, your Honor. Precisely.

7 THE COURT: Well, first of all, on the timing issue,  
8 that's an application that would be need to be made to Judge  
9 Pauley and not to me because he has not referred this case to  
10 me for general pretrial supervision, he has referred it to me  
11 for this discrete dispute. So, I am responsible in the first  
12 instance for resolving this dispute. And I am not suggesting  
13 that going to Judge Pauley might not be an appropriate thing to  
14 do, indeed that may be the right thing to do here, but I think  
15 we need to develop the record a little bit more.

16 What can you tell me about the what the SEC has  
17 received from Canadian regulatory authorities here and how does  
18 that dovetail with what you are otherwise seeking either from  
19 Vermont or the SMV?

20 MR. COSTELLO: Certainly, your Honor.

21 We have received three categories of documents from  
22 the Canadian regulator, the first category is trade blotters  
23 for or trade blotters for one of the securities in question and  
24 I have a copy of it, I can kind of just show the Court.

25 THE COURT: Can I ask, is it correct and maybe I am

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1 misremembering what I read, but I thought Verdmont's counsel  
2 was suggesting the Canadian regulators only have this  
3 information because they must have gotten it from the SMV. Is  
4 that your understanding as to where it came from? Or do you  
5 not know?

6 MR. COSTELLO: I truly do not know, your Honor. All I  
7 can tell you is that these documents came from the British  
8 Columbia Securities Commission. Whether the BCSC, as it is  
9 abbreviated, got those from Verdmont or whether they got those  
10 from the SMV, whether there exists some kind of agreement  
11 between Canada or one of the provincial regulators and the SMV  
12 I can't speak to that because I simply don't know.

13 THE COURT: How did the SEC obtain this information  
14 from the Canadian authorities? You made a specific request for  
15 them thinking that they might have some of this information?

16 MR. COSTELLO: As I understand it, yes, your Honor.  
17 And again, I'm not sure of the specifics on how that happened  
18 or whether that was done through a treaty with Canada or what  
19 have you and, again, I am concerned that we may be getting far  
20 afield from where we need to be in this instance.

21 THE COURT: Well, we are and we are not in the sense  
22 that obviously the bottom line here is what remains to be  
23 produced.

24 MR. COSTELLO: Certainly, your Honor.

25 THE COURT: I am assuming that some of what you are

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1 seeking from Verdmont or what you were seeking from Verdmont in  
2 these 10 categories was produced to you through the Canadian  
3 regulatory authorities; is that not right?

4 MR. COSTELLO: That is correct, your Honor. And I was  
5 going to tell the Court what we have received.

6 THE COURT: So that's, in some respect, narrowed what  
7 still remains to be produced; is that not right?

8 MR. COSTELLO: That is true; yes, in a sense; no, with  
9 a but, and I will explain, if the Court would allow me to.

10 THE COURT: All right.

11 MR. COSTELLO: The first category is trade blotters  
12 and it is not necessary to enter this but it is basically a  
13 trade blotter that has a list of the particular customers and  
14 the trades that they placed in the particular security and  
15 which clearing broker cleared those trades ultimately at the  
16 end of the transaction.

17 THE COURT: Names of the customers are identified?

18 MR. COSTELLO: Some of the customers' names are  
19 identified. Now let me just clarify what this is and what this  
20 isn't.

21 This particular plotter that I have in my hand here  
22 pertains to the Goff Corporation, that is one of the securities  
23 at issue. All of the other blotters that we got from the  
24 Canadians concern securities that are unrelated to this case; a  
25 number of them, in fact a couple dozen, to be frank. But there

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1 was no blotter for Xumanii and no blotter for Norstra.

2 I would also point out that this blotter that we got,  
3 this piece of paper that I have in my hand, is an excerpt,  
4 unfortunately, of all of the trades during the relevant period.  
5 For example, the first trade on here begins on March 18 of 2013  
6 and the last trade listed on here is April 3rd of 2013, but the  
7 Goff trading extended beyond April into June. That's the last  
8 time that the very last trade was made that sunk the price back  
9 to its penny stock value of cents on the dollar.

10 So, this appears to be a snippet of a point in time.  
11 I'm not sure why this is a snippet of a point in time, I'm not  
12 sure where the rest of it is.

13 THE COURT: The rest of it was not produced.

14 MR. COSTELLO: The rest of it was not produced, your  
15 Honor. And so, this is an example of -- so, this would be one  
16 trade blotter or, I should say, a portion of a trade blotter  
17 that really isn't telling us something that we didn't already  
18 know. So, that's the first.

19 THE COURT: How did you already know it?

20 MR. COSTELLO: Well, Vermont itself had given us  
21 other documents that basically provided the same information as  
22 this trade blotter did.

23 THE COURT: But not with the names of the customers  
24 who didn't provide waivers.

25 MR. COSTELLO: Some of the customers, and then the

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1 other customers, their account number is there. So, that is  
2 some information that we have but, again, not all of the  
3 information.

4 What I am just trying to get across to the Court is  
5 that -- and I will go into the second and third categories in a  
6 minute, that just because we received some things from the  
7 Canadian regulator doesn't mean we have everything.

8 THE COURT: I assume if you had everything we probably  
9 wouldn't be having this argument.

10 MR. COSTELLO: We would not be having this argument,  
11 your Honor, correct. Which is where I get back to what I said  
12 that I am hopeful that we can get this information from the  
13 Panamanian regulator and hopefully moot the need for any of  
14 this.

15 THE COURT: But you have no projected timeline so if  
16 you make an application to Judge Pauley to extend the April 0th  
17 date you are going to ask him to extend it indefinitely? He  
18 obviously won't do that so what period of time would you seek  
19 to extend it to?

20 MR. COSTELLO: What I would suggest, and I am not sure  
21 how the Court would prefer to handle this, but if the Court is  
22 going to do a report and recommendation, perhaps the Court  
23 could suggest to Judge Pauley maybe on a rolling basis. So,  
24 for example, the discovery period ends April 30th. Perhaps the  
25 Court could recommend to Judge Pauley that the deadline be



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1 pushed back just two months until June 30th, we will see where  
2 we are at that point -- hopefully we are somewhere -- and then  
3 if we don't need any more discovery or we have everything we  
4 have and there is no longer a dispute, then we don't need to  
5 push it back any further.

6 THE COURT: Well, to be clear, I'm not sure  
7 procedurally that's how it would go because the discovery  
8 dispute before me I would not be resolving on a report and  
9 recommendation basis, I would be issuing an order which either  
10 side could appeal from to Judge Pauley. But I wouldn't be  
11 doing a report and recommendation to him and resolving this  
12 dispute, however I do, nor would I be making a recommendation  
13 one way or the other about an extension.

14 If the upshot of today is we are going to hold this  
15 discovery dispute in abeyance while you make an application to  
16 Judge Pauley, then that's how we will deal with it,  
17 procedurally, just to be precise on that point.

18 Do you follow me?

19 MR. COSTELLO: I do, your Honor, and we can certainly  
20 go that route.

21 THE COURT: Can I ask you this question? Between now  
22 and April 30th, if there is no extension, what else is going to  
23 be going on in this case? Will there be depositions between  
24 now and the end of April that have not yet been taken place but  
25 have been scheduled or will be scheduled?

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1 MR. COSTELLO: Yes, your Honor, there will be  
2 depositions that will be taken.

3 THE COURT: Of whom?

4 MR. COSTELLO: As of now we will be taking the  
5 depositions is Vermont's principals Mr. Fisher and Mr.  
6 Housser, and the parties have scheduled those to take place in  
7 London in the United Kingdom on April 6th and April 7th.

8 THE COURT: What impact, if any, does this outstanding  
9 or open discovery have on those depositions? Anything? Other  
10 than, let me just say, all lawyers always want to have every  
11 piece of paper that would potentially be implicated in further  
12 litigation when they take depositions knowing full well that  
13 that is almost never a reality.

14 So, without that broad concept in mind what, in  
15 particular, about these outstanding requests, would have an  
16 impact, if any, on those depositions? Anything?

17 MR. COSTELLO: Well, your Honor, it would certainly be  
18 nice to have the documents in advance of the depositions but.

19 THE COURT: What if you don't?

20 MR. COSTELLO: We are still planning to proceed with  
21 the depositions.

22 THE COURT: And won't there be plenty else to ask them  
23 even without these documents?

24 MR. COSTELLO: There will be enough to ask, your Honor  
25 but, again, I just want to make sure that the Court is aware

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1 that we are not contending nor I believe have we contended that  
2 one is dependent on the other.

3 THE COURT: No, I know that. What I am trying to  
4 figure out is what is going to happen between now and April  
5 30th independent of the resolution of this discovery dispute.  
6 That's what I want to understand better.

7 So, you have the deposition of the two principals.  
8 What else?

9 MR. COSTELLO: There may be some additional  
10 depositions that the SEC will want to take. There may not be.  
11 I don't have a sense right now for what that's going to look  
12 like. We are still considering.

13 THE COURT: You are six weeks away from the end of  
14 discovery so I would think you would have some sense of what it  
15 is going to look like because you are going to run out of time  
16 otherwise.

17 MR. COSTELLO: Well, we are still discussing our  
18 options, your Honor. We are still discussing strategy. But  
19 again, even if the depositions that we took were limited to  
20 Mr. Fisher and Mr. Housser, the existence of the pending  
21 outstanding document dispute doesn't have any impact on that in  
22 the sense of that still is not something that we can control if  
23 we are going the SMV route. If we are waiting for the SMV to  
24 give the documents to us we don't have control over what they  
25 do over the next six weeks.

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1           What we were suggesting to the Court is if for  
2           whatever reason the discovery deadline can't be pushed back,  
3           then there is really no other alternative than to get these  
4           documents from Vermont and either go through a comity analysis  
5           or not go through a comity analysis or what have you.

6           THE COURT: Well, let's assume we deal with all of  
7           this on the merits -- and I am confident in telling you that I  
8           am not going to rule today on the merits but I would try to  
9           rule as promptly thereafter as I could. Whoever doesn't win is  
10          going to appeal to Judge Pauley and then you are going to give  
11          Judge Pauley some version of this -- the record should reflect  
12          I am holding a stack of records some inches deep -- and that  
13          will run its course up until April 30th. And then, no matter  
14          what, I guess Judge Pauley would have to extend, in some  
15          respect, if he rules that there should be production. And if  
16          he didn't, that would be the end of it.

17          So, I suppose in some respects that is a neater and  
18          cleaner way to proceed except that the clock may run out in  
19          that scenario.

20          What I am trying to figure out is if you clear the  
21          field, if you will, so that the only outstanding issue is this  
22          document production, that may be more appealing to Judge Pauley  
23          for one thing and would give me a better understanding of why,  
24          to use an expression, putting a pin in this dispute while we  
25          let the SMV process run its course, at least for some period of

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1 time to see what happens and having a further status conference  
2 to see whether this should or shouldn't be resolved may be the  
3 better way to go. I don't know.

4 MR. COSTELLO: I think we can certainly tell the Court  
5 now with some sense of confidence that the depositions that we  
6 have scheduled will probably still -- will go forward on April  
7 6th and 7th even if the document dispute isn't resolved at that  
8 point. And then, if the Court at that point were to say that  
9 maybe put a pin in this so that we can see what happens with  
10 the SMV, I think we would be comfortable with that. Otherwise,  
11 we wouldn't have offered that to the Court. I mean, I think  
12 that's probably the easiest way to go and it seems to be the  
13 least intrusive way to go. But, again, as we have said in our  
14 filings, we are just concerned that the deadline is not going  
15 to get pushed back and then we are in a little bit of a pickle  
16 having not done anything now when we could have.

17 THE COURT: Well, let me ask something else.

18 Aside from the two scheduled depositions and any other  
19 depositions that may be scheduled what else, if anything, is  
20 outstanding as far as discovery is concerned? Anything?

21 MR. COSTELLO: I believe that's it, your Honor.

22 THE COURT: So, April 30th will come and leaving aside  
23 this issue, depositions will be concluded and then Vermont is  
24 going to make a summary judgment motion. That's my  
25 understanding from colloquy and the papers.

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1 Is that not right, Mr. Zito?

2 MR. ZITO: That's correct, your Honor.

3 THE COURT: All right. Mr. Costello, why don't you  
4 sit down for a minute.

5 Mr. Zito, let me ask you this. I am assuming you are  
6 going to make a summary judgment motion on some relatively  
7 quick timeline after discovery closes 30 days thereafter or  
8 thereabouts, whatever you work out with Judge Pauley.

9 MR. ZITO: Yes, your Honor.

10 THE COURT: Does this document production issue that  
11 we are working through now have an impact on your motion?

12 MR. ZITO: Absolutely not.

13 THE COURT: Okay.

14 Is there any document that you would be relying on for  
15 your motion that has not otherwise been produced to the SEC?

16 MR. ZITO: No, your Honor.

17 THE COURT: No.

18 MR. ZITO: No.

19 THE COURT: Okay.

20 And, Mr. Costello -- Mr. Zito, you can sit again --  
21 Mr. Costello, do you have any sense that any of these documents  
22 we are talking about would be necessary to your opposition of  
23 Vermont's summary judgment motion?

24 MR. COSTELLO: Oh absolutely, your Honor.

25 THE COURT: So, flesh that out for me a little bit.

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1 MR. COSTELLO: Well, your Honor, I'm not sure exactly  
2 what their motion is going to look like but assume, for  
3 argument's sake, that they're going to move for summary  
4 judgment on the broker's exemption under Section 4.4 in the  
5 Exchange Act. The broker's exemption is a fact-specific  
6 exemption that depends on the level of controls that a  
7 broker-dealer has in place to ascertain whether or not its  
8 customers are colluding with issuers to engage in massive,  
9 illegitimate distributions of securities and there are a number  
10 of factors that Judge Pauley aptly laid out in his November  
11 opinion as to what that means. There has to be a reasonable  
12 inquiry that a broker-dealer is making and that inquiry looks  
13 at, for example, when the orders from its customers are placed,  
14 how soon or how long before the actual trading are those orders  
15 received, are orders from multiple customers being received on  
16 the very same day, are orders to sell matched with orders to  
17 buy. In other words, if one customer is wanting to unload a  
18 million shares of Norstra and another customer on the very same  
19 day is trying to buy a million shares of Norstra. That's  
20 probative of the question of whether the control were in place.

21 There is also the question of overlapping principles  
22 in IBC. Also the question of proceeds after the sales were  
23 done, after the net proceeds were realized and they were  
24 transferred from the clearing broker in the United States back  
25 to Verdmont in Panama? How did Verdmont disburse these

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1 proceeds? The wire transfer information so if there was  
2 \$50,000 in net proceeds made after commissions were taken out,  
3 were those proceeds wired to their customer, whoever that was  
4 on paper? Were those proceeds wired to someone else, perhaps a  
5 principal of that customer who overlaps into 10 different  
6 customers? What is the relationship between those principals  
7 and principals of Verdmont themselves who were trading in the  
8 securities? Did the principals of Verdmont trade in orders in  
9 advance of their customers?

10 The list goes on but just using that as an example,  
11 the documents that we have asked for in the 10 categories, for  
12 example one of the categories concerns orders, tickets and  
13 messages. Documentation. When these orders were placed. That  
14 type of information would assess whether Verdmont had  
15 sufficient controls in place.

16 THE COURT: Did you get any of those documents from  
17 the Canadian regulatory authorities?

18 MR. COSTELLO: No, we did not, your Honor, and that's,  
19 to come back to that trade blotter, this particular trade  
20 blotter is a blotter in the sense that it's more of a  
21 spreadsheet summarial-type document that has some columns in  
22 it, but in a broker-dealer brokerage in their record-keeping  
23 system there would be a series of additional columns on here.  
24 For example, the date the order was placed, the date the  
25 instruction was received, how the order was received, and



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1 Vermont, according to Vermont's own internal procedures and  
2 the account agreement that it has with its clients, it  
3 specifically says in there that Vermont will maintain a  
4 rigorous -- is the term that they use in there -- log of how  
5 they get these orders from their customers, when they get these  
6 orders, and will keep that log in what they say is  
7 chronological order. They then will send confirmations of  
8 these trades that the customers are placing within 24 hours.

9 That information the Canadians did not give us and,  
10 consequently, that is one of the categories of information that  
11 we are seeking here and hopefully the SMV has that information.

12 But, that's to give the Court a flavor of what we  
13 would need in order to have an opposition.

14 THE COURT: When you say hopefully the SMV has these  
15 documents, I think if -- and certainly Judge Pauley would be  
16 unhappy if I deferred any resolution of this -- you sought and  
17 got an extension from him, there was ultimately a production to  
18 the SEC, and some significant part of the information you were  
19 seeking wasn't produced to you because the SMV didn't have it.

20 So, I am a little concerned about your use of the word  
21 "hopefully." I mean, what makes you think they do have it?

22 MR. COSTELLO: That's just it, your Honor, I don't  
23 know whether they have it or not. Vermont has represented  
24 how -- its liquidator had represented that the SMV does but I  
25 don't have any way of independently verifying whether that's

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1 the case. That's why I am saying I am hopeful that what  
2 Vermont has represented is true and Vermont seems very  
3 confident that that's the case but until I can see what the SMV  
4 gives me I have no way of verifying that.

5 THE COURT: Well, when the SEC made its request of the  
6 SMV on February 24th, did it do so and communicate that in the  
7 court in the United States there was currently an April 30th  
8 deadline, so the sooner they could get to this the better it  
9 would be all around? Or some equivalent of that?

10 MR. COSTELLO: What we did is, your Honor, trying to  
11 be as respectful as possible of a foreign regulatory body, we  
12 intimated that time is a concern. But, again, we do not have  
13 any control over how a foreign regulatory body responds to a  
14 request for information. We simply don't know what's going to  
15 happen and we don't know how long it's going to take as I have  
16 been told by my Office of International Affairs.

17 THE COURT: And I gather, just to come full circle  
18 although I suspect I know the answer to this, a letters  
19 rogatory is not a realistic possibility here given the  
20 inevitable length that that usually takes.

21 Is that a fair and accurate statement?

22 MR. COSTELLO: That is a fair statement, your Honor.

23 Also, we did present all of these issues in the  
24 discovery plan that the parties had prepared jointly back in  
25 December. We flagged all of these issues. We said that there

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1 are some concerns with trying to get information out of a  
2 foreign country. Letters rogatory is an option but that's  
3 going to take a minimum of a year which is why we originally  
4 had proposed a longer discovery period. It was Vermont that  
5 wanted a March 30 deadline and it was the Court, ultimately,  
6 that set an April 30 deadline.

7 Now, we had said that we would be fine with a March 30  
8 deadline if Vermont's principals submitted to a deposition,  
9 which they have agreed to do, and if Vermont produced all the  
10 documents to us which unfortunately hasn't been done and  
11 doesn't look like it is going to be done, at least not  
12 voluntarily.

13 THE COURT: It is not going to be done voluntarily  
14 because they say Panamanian law prevents them from doing it and  
15 then we get into that issue.

16 MR. COSTELLO: And that's the conundrum, your Honor.

17 THE COURT: Mr. Zito, I have let Mr. Costello make a  
18 lot of arguments and address a lot of my questions. What do  
19 you want to say to me about any or all of these issues? What  
20 are your thoughts?

21 MR. ZITO: Your Honor, let me start with what the  
22 motion for summary judgment is going to look like.

23 Mr. Costello, the SEC has always skipped over the main  
24 defense of this case which is the so-called dealer's exemption.  
25 They talk about this broker's exemption but they never once

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1 ever implied as to why the dealer's exemption doesn't apply  
2 here, and it applies because if you didn't have a dealer's  
3 exemption virtually every transaction where there is a  
4 registration statement that was filed would be subject to a  
5 Section 5 violation. So, Congress enacted this dealer's  
6 exemption to prevent constant litigation over every trade such  
7 as these.

8 So, if we focus on what that dealer's exemption is, it  
9 is very simple. Okay? If trades in the securities happen more  
10 than 40 days after the registration statement is declared  
11 effective by the SEC, if the trade happens in more than 40  
12 days, then the transaction is exempt. Section 5 doesn't apply.  
13 And in each of these cases a registration statement was on  
14 file, the SEC itself declared them effective, and each and  
15 every one of these trades took place after that 40-day period.

16 THE COURT: Well, we are not here to argue your  
17 summary judgment motion. I am certainly not prepared to do  
18 that. But, the SEC has a different theory about registration,  
19 right?

20 MR. ZITO: Right.

21 THE COURT: It has to be pre-registered, effectively,  
22 as I understand their position. Is that not right?

23 MR. ZITO: According to the amended complaint they're  
24 saying, well, this was all a sham because the securities never  
25 came to rest with the public because it was all with

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1 individuals, it was all with insiders and people in the  
2 control. They've never produced any evidence of that but they  
3 say it in the complaint.

4 THE COURT: Okay.

5 MR. ZITO: And I assume that's what they're going to  
6 prove or what they're trying to prove.

7 THE COURT: They'll have to put something in the  
8 record before Judge Pauley in that point in opposition to your  
9 motion, presumably.

10 MR. ZITO: So then what they're going to have to say,  
11 they're going to have to disprove that that 40-day period  
12 doesn't start to run until some later period, although they've  
13 never explained to us what that later period is but that's what  
14 they would have to prove. So, it is a timing issue. It has  
15 nothing to do with these trades.

16 But, let me now turn over to the dealer's exemption  
17 which is the broker's exemption which is the second. We don't  
18 get to the broker's exemption unless they're able to prove that  
19 this was all a sham and they've taken not a single deposition  
20 in this case of anyone who has testified that they were a sham  
21 or that they were insiders, that the trades were made to  
22 affiliates. And they haven't served any notices to take  
23 depositions. They said we wanted to take letters rogatory, we  
24 want to take testimony of people in Ireland, in Belize, in  
25 Bulgaria.

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1           They have never obtained any letters rogatory and that  
2           is at the heart of their case. They have to prove this sham  
3           theory what they themselves plead in the amended complaint.  
4           So, they haven't done that so I am confident, your Honor, that  
5           we are going to prevail on the dealer's exemption but let's now  
6           move to the broker's exemption.

7           THE COURT: Well, I don't want to belabor this too  
8           much because the reason why I asked about the summary judgment  
9           motion was only because I was trying it figure out what the  
10          relationship, if any was, between the discovery that is at  
11          issue right now and what is going to transpire once discovery  
12          closed whether it is April 30th or any other date.

13          MR. ZITO: And as I think your Honor can see, the only  
14          proof that's germane to the dealer's exemption is when was the  
15          registration statement filed, that the Court can take judicial  
16          notice of off of Edgar when the registration statement was  
17          deemed effective. Again, that's on the SEC Edgar website, the  
18          Court can take judicial notice of that. And, thirdly, when did  
19          the trades take place? And we have produced all the documents  
20          as to when those trades took place. Okay?

21          So, those three pieces of fact demonstrate that all  
22          the transactions took place after the 40-day waiting period.  
23          All right? The transactions are exempt. All right? None of  
24          the documents that Mr. Costello is referring to had anything to  
25          do with this dealer's exemption. They have nothing to do with

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1 it.

2 THE COURT: Is Vermont, for purposes of summary  
3 judgment, accepting that the SEC has established a prima facie  
4 case under Section 5?

5 MR. ZITO: Your Honor, it is very --

6 THE COURT: In other words is the discovery here, if  
7 it is relevant, relevant to the defenses, not to the Section 5  
8 violation, per se?

9 MR. ZITO: The law requires us to prove an exemption.  
10 The law requires us to prove an exemption and we have proved  
11 the exemption and we will continue to prove the exemption by  
12 those three facts and those are undisputable facts and we will  
13 prove those facts.

14 For them to now at that juncture, the burden of proof  
15 shifts back to them to say, well, it is not really a 40-day  
16 period because something else happened, there was a simulated  
17 offering which they allege, they say there was a simulated  
18 offering because that 40-day period shouldn't start to run  
19 there, it should start to run at some later period, although  
20 they never specify what that later period is because this was  
21 all a sham and they say this in the most conclusory way. All  
22 right? This is all a sham.

23 Once we have proved the 40-day period they then have  
24 to prove that the 40-day period really isn't a 40-day period  
25 because there was some sham going on and I don't know how they

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1 prove that. They certainly don't prove it by trade blotters.

2 And, your Honor, while we are talking about trade  
3 blotters, we produced all the trade blotters. We produced, in  
4 excruciating detail, all these blotters showing exactly when  
5 the trades happen, the volume of the trades, and the exact  
6 dates.

7 So, I don't know what all of this has to do with the  
8 40-day waiting period and that's what this case -- it is nice.  
9 It is interesting, I guess, but it is not going to relate to  
10 the depositions. It is not going to relate to the summary  
11 judgment motion.

12 THE COURT: What is your view as to how we should  
13 proceed?

14 MR. ZITO: Your Honor, this case has been banging  
15 around for a year. It seems to me that if the SEC was sincere  
16 about being interested in these documents, they could have  
17 gotten them from the SMV or they could have at least initiated  
18 a request or an MOU. I mean, your Honor, what they say here is  
19 that the SEC and SMV are not parties to any treaties or other  
20 formal bilateral agreements but they didn't mention the fact  
21 that there is an MOU.

22 THE COURT: Well, there wasn't one until recently, it  
23 sounds like.

24 MR. ZITO: Well --

25 THE COURT: And they felt that they couldn't ask in



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1 any formal way for any assistance unless and until there was  
2 one. So, that's their position on that.

3 MR. ZITO: Well, they could have asked -- well, then  
4 fine. Then they have to make a case as to why the discovery  
5 cutoff should be extended. What is the good cause for that?

6 THE COURT: Well, the good cause is it may take the  
7 SMV longer than another two weeks to process this request.

8 MR. ZITO: And I will come back with, one, delay,  
9 because they could have done this -- they haven't -- I haven't  
10 heard as to a reason why they didn't make the request a year  
11 ago if they haven't made a request a year ago. I'm being told  
12 that there was an exchange of information that goes back to  
13 April of last year.

14 Also, your Honor, I want to be very clear here, that  
15 we did not produce documents, Verdmont did not produce  
16 documents to the Canadian regulators. They only gave documents  
17 to the Panamanian regulators. The SEC got documents from the  
18 Canadian regulators who got the documents from the Panamanian  
19 regulators. And they've had these documents for months, your  
20 Honor.

21 THE COURT: Well, let me ask you this. If discovery  
22 is scheduled to conclude on April 30th, and you are going to  
23 file a motion for summary judgment on May 30th, and the SEC's  
24 opposition to that motion is going to be due June 30th, why  
25 shouldn't we extend the discovery solely for the purpose of

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1 seeing whether the SMV produces these documents to the SEC by  
2 May 30th and have a status conference at that time and then see  
3 if it has. That may be the end of it. And if it hasn't, then  
4 what they may choose to do is under Rule 56 invoke the  
5 provision of we can't fully respond until we have this  
6 discovery. Or, they may decide they don't need it because they  
7 can fully respond to the motion.

8 MR. ZITO: That's why we could make the motion.

9 THE COURT: So I am responding to your delay point  
10 which is nothing will be delayed if discovery ends April 30th,  
11 you make your motion by May 30th, we have a conference on May  
12 31st and I am advised then or before then this worked out with  
13 the SMV, this hasn't worked out with the SMV, we have a  
14 timeline from the SMV, whatever is known. That's more than two  
15 months from now and I assume the SEC is going to say, in the  
16 most polite, diplomatic way possible to the SMV this case is  
17 moving forward and if you can do anything to expedite your  
18 process it will be of great assistance. And however they would  
19 do that, one regulator to the other, in the same way I am sure  
20 in some circumstances the Panamanian authorities will need the  
21 American authorities to do the same. That's why you enter into  
22 such MOUs. But, meanwhile, you are not delayed because these  
23 depositions that you all agreed to are taking place in April,  
24 the discovery deadline remains April 30th, you make your motion  
25 on May 30th, and then on May 31st, with the expectation that

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1 the SEC is going to respond to your motion on June 30th, we  
2 then have a discussion perhaps first with me on this point and  
3 then secondarily with Judge Pauley, depending on how it shakes  
4 out if the schedule changes. And I am putting these dates out  
5 there without authority from Judge Pauley so he may not abide  
6 by this but I certainly, to Mr. Costello's point, would  
7 recommend it given sort of the posture we are in now.

8 What about that as a scenario?

9 MR. ZITO: My response is two-fold.

10 One, as long as I'm not being delayed from making my  
11 motion for summary judgment, okay, and because there is  
12 \$250,000 -- Vermont is in liquidation. It is going to cease  
13 to operate, it is losing money at the rate of \$200,000 a month.  
14 The more this continues to get delayed, the more of the  
15 probability that my ability of getting paid and being able to  
16 defend Vermont starts to run out. So, we have got a short  
17 window here under the liquidation. If the SEC is able to drag  
18 this out as long as possible they know that the cash will dry  
19 up and I'm not going to get paid and I'm not going to stay in  
20 this case if I'm not getting paid. They know that.

21 THE COURT: Why is that in the SEC's interest?

22 MR. ZITO: Because if I am not in the case then they  
23 can move for a default and they can get a default judgment and  
24 say we won.

25 THE COURT: Which will be worth what?

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1 MR. ZITO: Well --

2 THE COURT: I'm not sure that's what this is about.

3 MR. ZITO: Well, I think it is, your Honor, because if  
4 you look at the Caledonian settlement, they settled the  
5 Caledonian case for zero, no money on the dollar. What they  
6 got -- what they got -- was an admission from Caledonian that  
7 the \$25 million that the SEC wrongfully froze was something  
8 that Caledonian was responsible for. That's what they got.  
9 And the reason why this case hasn't settled is because they  
10 want us to admit that their initial freeze order that was  
11 illegal, based on misrepresentations to Judge Pauley, that that  
12 \$17 million was something we were responsible for.

13 That's what this is all about.

14 THE COURT: Okay. Well --

15 MR. ZITO: And, your Honor --

16 THE COURT: But to your point, you are not going to be  
17 delayed by my proposal, are you? I mean, you wouldn't be  
18 making summary judgment motion any sooner than the schedule I  
19 am suggesting.

20 MR. ZITO: By that timeline, your Honor, no. But I am  
21 not sanguine as we have seen how these things drag on as if  
22 there is always something else and maybe there is something  
23 else and then there is another delay and another delay.

24 Under the guidelines, under the timetable your Honor  
25 just set forth, no, as long as I'm not being delayed on the

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1 motion.

2 I also want to point out, your Honor, that we have  
3 voluntarily agreed to deposit and freeze \$240,000. We are  
4 going to need access to that \$240,000 -- my firm is going to  
5 need access to that \$240,000 so that we can continue to  
6 represent Vermont in these protracted proceedings.

7 THE COURT: Well, that's outside the scope of my  
8 referral so you will have to talk to Mr. Costello about that  
9 and you may have to talk to Judge Pauley about that.

10 MR. ZITO: We are in the process of writing Judge  
11 Pauley about that, your Honor. We asked the SEC to consent to  
12 that and they haven't consented to that. So they don't want to  
13 consent to freeing up the money but they want us to consent on  
14 extending deadlines.

15 THE COURT: This is my proposal, this is not their  
16 proposal, so as far as I'm concerned we are not extending the  
17 discovery deadline, we are keeping it in place. You are taking  
18 the two depositions that are already scheduled and any other  
19 depositions that are properly noticed between now and April  
20 30th. April 30th comes, discovery is over. You make a motion.  
21 The 30th is Memorial Day so I will say the 31st of May, right?  
22 And then the SEC's response is due June 30th, 30 days later.  
23 And then you reply two weeks thereafter, you have a fully  
24 submitted motion before Judge Pauley by July 14th.

25 That's about as fast as you could do on this schedule

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1 and that hasn't moved the April 30th date at all which, in my  
2 experience, when a date is set in a case like this it almost  
3 always moves. So, it is not moving the date.

4 Now, there is a footnote. The footnote is if your  
5 papers are due May 31st we will need to schedule now a status  
6 conference that week, of the week of May 31st, so I can be  
7 fully apprised of the status of this issue which I am  
8 effectively leaving open which I am not that keen to do,  
9 frankly. But, it seems to me that if the SMV is going to  
10 produce all of this information and produce it on May 31st, it  
11 seems unwise in the extreme to me for me to issue a decision,  
12 whoever I rule against taking an appeal of that decision to  
13 Judge Pauley, us all trying to work at rapid-fire speed only to  
14 have that superseded by the production that all here have  
15 agreed would moot the question.

16 So, that's why I am suggesting we proceed this way.

17 MR. ZITO: Your Honor, like I said, we have no  
18 interest in preventing the SEC from getting information. They  
19 can get information and they have been getting information  
20 without our help and I have no problem with them continuing to  
21 get information. If they get it a day after discovery cutoff I  
22 am not going to say, oh, you can't use that because you got the  
23 information a day after the cutoff. I mean, that's certainly  
24 not in our interest. Our only interest again is in delay and  
25 making a summary judgment motion as soon as possible. That's

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1 our interest.

2 THE COURT: All right.

3 Mr. Costello, on May 31st, if you don't have this  
4 information and we have a conference on June 1st, what will  
5 happen then?

6 MR. COSTELLO: Well, your Honor, I guess that depends  
7 on what --

8 THE COURT: What you know from the SMV at that point?

9 MR. COSTELLO: Well, I mean, if we don't have the  
10 documents from the SMV then I guess I would ask the Court then,  
11 I suppose we would pick up at that point to the question of  
12 whether Vermont should be required to produce the documents  
13 and then I guess we will have to get into the comity analysis.

14 But, I guess I am just concerned because this would be  
15 on June 1st which is now a month after the close of discovery,  
16 then couldn't Vermont simply say at that point well, discovery  
17 is closed?

18 THE COURT: Well, no, because it would be closed  
19 subject to this issue being resolved. So, the production, if  
20 it is to be ordered either by me and/or Judge Pauley or not,  
21 will obviously post-date the April 30th date but I'm trying to  
22 hedge our bets collectively, if you will, because if the SMV  
23 makes this production to you, it doesn't do it neatly before  
24 April 30th but does it in mid-May, let's say, it doesn't seem  
25 wise for the judicial apparatus, if you will, as well as you

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1 all, to continue to litigate this question when it would be  
2 mooted and you have some expectation, it seems to me, that that  
3 could happen.

4 It is not unlikely. I mean you can't predict, I  
5 understand that. I'm not committing you to the expectation  
6 that it will definitively be produced by the SMV. And, as far  
7 as I'm concerned, in some respects if I issued a decision 10  
8 days from now I would be done with this but I don't know that  
9 that's the most practical way to proceed because if I were to  
10 issue a decision on March 25th, let's say, and there are two  
11 weeks to file objections and you all file objections by the  
12 14th day which is early April, April 8th or whatever it might  
13 be, and by the time Judge Pauley gets to it he might have to  
14 write his own decision, we are at April 30th.

15 So, I am not sure that scenario takes us to a better  
16 place is my point. And I am not trying to shirk any  
17 responsibilities because I am more than happy to write a  
18 decision in this matter and we have been working on one, to be  
19 candid with you, but I also want to be practical because that  
20 makes the most sense. And I also want to be mindful of the  
21 dictates of Rule 26, among other things, which requires even a  
22 greater emphasis on proportionality as you all know we focused  
23 on, and there are some separate issues about that since we do  
24 have a company that is in liquidation and I don't know what  
25 burden there would be here as far as putting Vermont to its



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1 proof in the state that it is in, at least that was represented  
2 to the Court. That is another issue that we have to air out  
3 and I am not sure we need to do that today.

4 Does anybody have anything else they want to offer at  
5 this juncture, counsel?

6 MR. COSTELLO: Nothing from us, your Honor.

7 THE COURT: All right.

8 Mr. Zito?

9 MR. ZITO: In closing, your Honor, I just want to  
10 emphasize that I strongly submit that the information that the  
11 SEC claims it doesn't have -- and I'm not even sure it exists  
12 to the extent that I have heard about these blotters -- I don't  
13 see how this relates in any way to the summary judgment or to  
14 any liability or any defense in this case.

15 THE COURT: All right. Well, I think I will allow you  
16 all to agree to disagree on that point and happily I don't have  
17 to resolve that particular point. I am more interested in the  
18 practicalities. Do I hear either side objecting to the  
19 scenario that I have proposed, if you will, where the discovery  
20 deadline would remain in place subject to resolution of this so  
21 it would post-date the discovery close but, in the meantime,  
22 the summary judgment schedule would run its course and then we  
23 would, once the defendant's papers are filed, we would have a  
24 status conference so I could revisit where this stood? And  
25 obviously if at any point between now and May 31st there was

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1 information that the Court needed to know, either the SMV had  
2 produced the information, the SMV had said it will not produce  
3 the information or anything like that, I assume that the SEC  
4 would provide both me and Judge Pauley for that matter and the  
5 defense whatever information they had.

6 MR. ZITO: I'm not opposed to that. Again, we only  
7 care about the filing of our summary judgment motion.

8 THE COURT: Right.

9 MR. ZITO: If that's not a bar to the filing of our  
10 summary judgment motion, I know that Judge Pauley requests that  
11 there be a pre-motion conference and in accordance with those  
12 kinds of deadlines we will request that motion conference  
13 immediately, the pre-motion conference immediately.

14 THE COURT: What I was thinking of doing is taking a  
15 short recess and seeing if I could get him on the phone and  
16 tell him where we are in all of this and see if he has any  
17 views. I don't know if he is in Court this afternoon or not.

18 So, why don't we take a short recess and let me  
19 attempt to do that.

20 MR. ZITO: Thank you, your Honor.

21 (Recess)

22 THE COURT: Mr. Zito, am I right in assuming that in  
23 your summary judgment motion you are going to rely on both the  
24 dealer's exemption and the broker's exemption, or are you just  
25 going to argue with respect to the dealer's exemption?

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1 MR. ZITO: I haven't decided that yet but --

2 THE COURT: I will tell you why I am asking.

3 It seems to me, unless I misunderstood Mr. Costello,  
4 that his focus on the relevance of these documents was with  
5 respect to the broker's exemption. That's what I heard today.

6 Is that not a fair statement? That's what you  
7 emphasized in your presentation today, Mr. Costello.

8 MR. COSTELLO: Your Honor, I spoke about the broker's  
9 exemption and then Mr. Zito took over after that. There is  
10 also --

11 THE COURT: You think they're relevant to both  
12 exemptions?

13 MR. COSTELLO: Yes, that's correct.

14 THE COURT: And you want the documents for both  
15 exemptions?

16 MR. COSTELLO: Correct, your Honor.

17 THE COURT: All right. So let's leave it there then.  
18 I was thinking that there was a faster path to resolution here  
19 which was that if Mr. Zito said I'm only going to move on the  
20 dealer's exemption and the SEC recognized that these documents  
21 really were far more relevant, if I can put it that way, to the  
22 broker's exemption, then it might narrow things. But, I gather  
23 you are not prepared to commit to any of that. You want to  
24 make your motion on both prongs, presumably, or you don't know  
25 yet and haven't decided and Mr. Costello is not willing to --

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1 MR. ZITO: They're somewhat entwined, your Honor, if I  
2 can just address it briefly.

3 The broker's exemption isn't -- what Mr. Costello  
4 seemed to be alluding to was suitability, whether or not these  
5 were suitable trades, know your customer and all that kind of  
6 thing. That's not what the broker's exemption relates to.

7 The broker's exemption relates to whether or not there  
8 were any red flags to know whether these stocks were not  
9 registered. And typically what every brokerage house does is  
10 that they go to the SEC database, they see if there is a  
11 registration statement on file, they see whether or not there  
12 is a registration that is effective and if you look at all the  
13 blotters it says checked SEC file, checked SEC file. Those are  
14 the kinds of things, that's the diligence they do. They don't  
15 look at whether other clients are trading in this, what time of  
16 day they're trading in it. All they want to know is are these  
17 trades happening in 40 days, is there something happening with  
18 the principals, do the principals appear to be insiders. They  
19 look at who the principals of the companies are and that's more  
20 or less the extent of the analysis.

21 THE COURT: That's fine. I think I opened up a can of  
22 worms.

23 Mr. Costello, suffice to say, you think these  
24 documents have relevance for both exemptions; is that correct?

25 MR. COSTELLO: Yes, your Honor. That's correct.

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1 THE COURT: And relevance, if you want to just say for  
2 the record with respect to the dealer's exemption, is what?

3 MR. COSTELLO: Well, the dealer's exemption hinges on  
4 whether the offering was a bona fide public offering. Judge  
5 Pauley has already delineated the standards for that and that's  
6 the question, is it a simulated offering or is it being  
7 genuinely offered to the public as part of a legitimate public  
8 sale.

9 So, in this instance, for example, your Honor, the  
10 certificates that were cleared came in 2011 and 2012. I don't  
11 know whether in Vermont's motion for summary judgment they're  
12 going to contend that the bona fide offering took place at that  
13 point, whether it took place at the time the registration  
14 statements were effective or some other point in time. But, if  
15 that's the point in time that they're going to argue, then we  
16 have the right to know, well, if this public offering was a  
17 legitimate offering, then there would be quotations, there  
18 would be bids, there would be prices, there would be asks. And  
19 if there is not -- and I'm going to represent that there wasn't  
20 to my knowledge -- then how did these clients get interested in  
21 these securities which at that point had never been traded  
22 before? How all of a sudden did they get interested in that?  
23 Were they making a market for these things? Were they  
24 matching? And again Mr. Zito is correct, the two exemptions do  
25 overlap in that sense. But, if multiple clients are all part

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1 of the same buy, trade, matched -- paint the tape as it is  
2 called, your Honor -- that goes to the question of whether this  
3 offering is simulated or whether it is bona fide. And I don't  
4 know what Mr. Zito is planning to argue in his motion but  
5 whatever it is, these documents hold the key to that.

6 MR. ZITO: I'm going to argue very simply, your Honor,  
7 that all the trades took place after the 40-day holding period.  
8 If the SEC believes that that 40-day period should start to run  
9 in some period of time, none of the documents they've requested  
10 go to that issue.

11 THE COURT: Okay.

12 I was able to reach Judge Pauley and he is amenable to  
13 the schedule that I have suggested to you all with the  
14 understanding, Mr. Zito, that when you submit your pre-motion  
15 letter you will reference the fact that this was the schedule  
16 that was proposed, and in fact I will put an order out on the  
17 docket to that effect with this schedule that we have in mind  
18 here. I plan to issue an order that will deny both motions  
19 without prejudice to their renewal, that I will schedule a  
20 status conference for the week of May 31st, that will set the  
21 schedule such that May 31st will be the date for the motion,  
22 assuming a pre-motion conference and any other requirement that  
23 Judge Pauley has is met, and subject to his modifying the  
24 schedule as he sees fit. And then the SEC will file its  
25 response by June 30th, and the defendant will respond by July

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1 14th.

2 If, in the interim, there is any developments with  
3 respect to the SMV's ability to produce this information to the  
4 SEC, obviously you would apprise both Judge Pauley and I of  
5 that fact is how I think I will leave it. Okay?

6 MR. COSTELLO: Yes, your Honor.

7 MR. ZITO: Thank you, your Honor.

8 THE COURT: Before I let you go, is there any other  
9 open issue relating to this dispute that I need to deal with,  
10 or does this resolve it satisfactorily at this juncture?

11 MR. ZITO: The only issue I have, your Honor, is  
12 whether we need to seal the transcript and, if so, to what  
13 extent, and I just quite frankly don't know the answer to that.

14 THE COURT: Well, does the SEC have any view about  
15 whether the transcript needs to be sealed?

16 MR. COSTELLO: I don't believe it does, your Honor,  
17 but if Mr. Zito is concerned and he wants to brief the issue or  
18 look further into it, then I propose he can but I don't see an  
19 issue with it.

20 THE COURT: Mr. Zito, you tell me.

21 MR. ZITO: Well, in an abundance of caution, your  
22 Honor, let's seal it.

23 THE COURT: Well, I'm not going to seal the whole  
24 thing.

25 MR. ZITO: Just the portions about the MOU, my

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1 understanding is that that is the -- well, then I will have to  
2 go through it.

3 Can I confer with my client, your Honor?

4 THE COURT: Can you confer with your client?

5 MR. ZITO: And can I notify the Court by tomorrow?

6 THE COURT: I assume that the transcript is going to  
7 be ordered, correct? And once it is ordered it will eventually  
8 get put on the docket. However, there is an interim period of  
9 time once the record is transcribed where parties can make  
10 objections or make requests, redactions, etc. So, in that  
11 intervening period of time if you have an application you  
12 should make it.

13 MR. ZITO: Thank you, your Honor.

14 THE COURT: And with respect to redactions, I  
15 assume -- there has been some discussion in all these papers  
16 about what was produced, some of which was redacted, some of  
17 which wasn't redacted. Do I need to reach any of that at this  
18 juncture? I just am raising that in an abundance of caution.  
19 Or, has that been sufficiently resolved?

20 MR. COSTELLO: Your Honor, I believe that if as  
21 Vermont said that the SMV has all of the documents then,  
22 presumably, the SMV would have all of these particular redacted  
23 documents in a non-redacted form and so, presumably, once we  
24 get the production from the SMV, we will see all of these  
25 documents in a non-redacted form. If we don't, then I guess we



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1 can take up the issue of the redactions along with the status  
2 conference the Court will hold.

3 THE COURT: All right.

4 Is there any particular day of the week, since  
5 Mr. Costello you are coming from Washington, yes?

6 MR. COSTELLO: Correct, your Honor.

7 THE COURT: Do you have a preference as to when you  
8 come up to New York? Does that matter one way or the other to  
9 you? Would you rather it be a Friday, for example, as opposed  
10 to some other day of the week? Is that better or worse?

11 MR. COSTELLO: If the Court has a Friday available,  
12 certainly that would be.

13 THE COURT: We will look at the calendar.

14 Dave, do you have the calendar in front of you?

15 So, Friday, June 3rd, shall we have a status  
16 conference then?

17 MR. COSTELLO: If your Honor would give me a moment  
18 just to check my calendar? Yes, your Honor, it appears that  
19 June 3rd would work.

20 THE COURT: Do you have preference for the morning or  
21 the afternoon?

22 MR. COSTELLO: The morning would be good, your Honor.

23 THE COURT: Shall we say 10:00?

24 MR. COSTELLO: Yes, your Honor. That sounds good.

25 THE COURT: Mr. Zito, does that seem okay with you?

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1 MR. ZITO: That's fine, your Honor.

2 THE COURT: All right. So, we will have a status  
3 conference on June 30 at 10:00. Obviously if events overtake  
4 the circumstances such that the conference is mooted, we will  
5 adjourn it if you provide a basis for us to do so, but  
6 otherwise, I will see you then and I wish you good luck, and be  
7 well until then.

8 MR. COSTELLO: Thank you, your Honor.

9 MR. ZITO: Thank you, your Honor.

10 THE COURT: Thank you, all.

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